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IN THE

Supreme Court of the United States

OCTOBER TERM, 1945.

No. 392

IN THE MATTER OF: THE CHICAGO, ROCK ISLAND AND PACIFIC RAILWAY COMPANY,

Debtor.

WALTER E. MEYER,

Petitioner,

vs.

JOSEPH B. FLEMING AND AARON COLNON, AS TRUSTEES OF THE CHICAGO, ROCK ISLAND AND PACIFIC RAILWAY COMPANY,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT, AND BRIEF IN SUPPORT THEREOF

WALTER E. MEYER,
Petitioner, *Pro Se*,
31 Nassau Street,
New York 5, N. Y.

SONNENSCHEIN, BERKSON, LAUTMANN,
LEVINSON & MORSE,
Attorneys for Petitioner,
77 West Washington Street,
Chicago 2, Illinois.

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vs.

JOSEPH B. FLEMING AND AARON COLNON, AS TRUSTEES OF THE CHICAGO, ROCK ISLAND AND PACIFIC RAILWAY COMPANY,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

To the Honorable the Chief Justice and Associate Justices of the Supreme Court of the United States:

Your petitioner respectfully shows:

Statement of Matter Involved

Your petitioner, a large stockholder and at the time a director of St. Louis Southwestern Railway Company

(hereinafter referred to as "St. Louis Southwestern"), on April 26, 1934, filed a claim for the benefit of St. Louis Southwestern, in proceedings under Section 77 of the Bankruptcy Act for the reorganization of The Chicago, Rock Island & Pacific Railway Company (hereinafter referred to as "Rock Island" or "debtor") instituted in the District Court of the United States for the Northern District of Illinois, Eastern Division (R. 2).

The claim is in the amount of $31,593,874, $29,126,874 being for damages arising out of successive conspiracies in which Rock Island was alleged to have participated, by which St. Louis Southwestern was wrongfully and illegally controlled from March 11, 1925, to June 7, 1933, the date of the initiation of the Rock Island reorganization proceedings, and $2,467,000 being the amount for which it is asked that Rock Island account to St. Louis Southwestern for profits which Rock Island realized in dealings in the stock of St. Louis Southwestern while illegally controlling that company (R. 2-7).

The claim was filed by petitioner in behalf of St. Louis Southwestern because at that time Southern Pacific Company controlled St. Louis Southwestern, and Southern Pacific Company and the directors of St. Louis Southwestern were co-conspirators with Rock Island in connection with the conspiracies by which St. Louis Southwestern was damaged (R. 3).

The trustees of Rock Island, respondents herein, on May 25, 1935, filed objections in the nature of a general denial of the said claim (R. 7).

On December 12, 1935, a year and a half after the filing of the claim, St. Louis Southwestern filed a petition for reorganization, under Section 77 of the Bankruptcy Act, in the United States District Court for the Eastern Judicial District of Missouri, Eastern Division. The Court

approved the petition, and on January 3, 1936, appointed a trustee for the company (R. 51).

Among the objections filed thereafter by the respondents was the objection that petitioner could no longer prosecute the claim because, by reason of the reorganization proceedings and the appointment of a trustee of St. Louis Southwestern, title to the causes of action set forth in said claim became vested in that trustee (R. 8).

The trustee of St. Louis Southwestern has made no step to take over the claim or to enjoin its prosecution by petitioner, nor have the respondents alleged that he has done so.

The claim having been referred to a Special Master, respondents and petitioner requested that the Special Master, before entering upon a hearing on the merits, first dispose of the objection of the respondents which raised the issue of petitioner's right to further prosecute the claim (R. 34, 50).

On February 2, 1942, the Special Master filed his report (R. 34-44) and supplemental report (R. 44-47), finding and concluding that petitioner should not be allowed to continue to prosecute the claim.

On February 7, 1944, the District Court entered its order approving the reports of the Special Master (R. 49-52), and on June 6, 1945, the Circuit Court of Appeals affirmed the order of the District Court (R. 61-66).

The Circuit Court of Appeals held that after the institution of reorganization proceedings and the appointment of a trustee of St. Louis Southwestern petitioner could no longer prosecute the claim. It based its decision, as had the District Court, on subsections (a) and (c)(2) of Section 77 of the Bankruptcy Act (R. 63).

Subsection (a) provides that the reorganization court shall have "exclusive jurisdiction of the debtor and its

property wherever located" and "in addition to the powers conferred by this section all the powers, not inconsistent with this section, which a Federal court would have had if it had appointed a receiver in equity of the property of the debtor for any purpose."

Subsection (c)(2) confers upon the trustee in a Section 77 proceeding the title and powers of a trustee "appointed pursuant to section 72 or any other section of this title [11 U. S. C. A.], and, to the extent not inconsistent with this section, if authorized by the judge, the powers of a receiver in an equity proceeding, * * *"

The Circuit Court was of the opinion that "the continuance without court permission" of the prosecution of the claim filed previous to reorganization proceedings was "inconsistent with those powers of exclusive management" (R. 65).

It is submitted that the Circuit Court wrongly construed subsections (a) and (c)(2) of Section 77 of the Bankruptcy Act, and that there is nothing in these subsections or in any other part of Section 77 which precludes the continued prosecution of the claim by petitioner.

Jurisdiction

The judgment of the United States Circuit Court of Appeals was entered on June 6, 1945 (R. 66).

The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code [28 U. S. C. A. 347(a)], as amended.

The Question Presented

A stockholder of a railroad corporation filed a claim for the benefit of his railroad in the reorganization proceedings of another railroad. Thereafter, the railroad for-

the benefit of which the claim was filed went into reorganization and a trustee was appointed. There being no action on the part of said trustee to take-over or restrain the prosecution of said claim, may the trustees of the railroad against which the claim was filed raise the objection that the initiation of reorganization proceedings and the appointment of a trustee of the railroad for the benefit of which the claim was filed, by virtue of subsections (a) and (c)(2) of Section 77 of the Bankruptcy Act, preclude the continued prosecution of the claim by the stockholder?

Statute Involved.

The statute involved is Section 77 of the Bankruptcy Act, and particularly subsections (a), (c)(2) and (*l*) thereof [11 U. S. C. A. 205 (a), (c)(2) and (*l*)]. The pertinent language of said subsections is printed in the Appendix, pages 26-27 hereof.

Reasons Relied on for Allowance of the Writ

1. The Circuit Court of Appeals in holding, upon the objection of the respondents, the trustees of Rock Island, that petitioner, a stockholder of St. Louis Southwestern, under subsections (a) and (c)(2) of Section 77 of the Bankruptcy Act was prevented from continuing to prosecute a claim filed by him in behalf of St. Louis Southwestern in the Rock Island reorganization proceedings previous to the initiation of proceedings for reorganization of St. Louis Southwestern, decided an important question of Federal law which has not been but should be settled by this Court.

2. The Circuit Court of Appeals in so holding decided a Federal question in a way probably in conflict with applicable decisions of this Court.

3. The Circuit Court of Appeals in so holding rendered a decision in conflict with decisions of the Circuit Court of Appeals for the Second Circuit, and probably in conflict with decisions of the Circuit Courts of Appeals for the Eighth, Ninth and Third Circuits respectively.

It is important that the Supreme Court pass upon the language of the statute in question inasmuch as the decision of the Circuit Court below affects the right of railroad corporations in reorganization proceedings under Section 77 and also other corporations under Chapter X of the Bankruptcy Act (formerly Section 77B), and of stockholders in representative actions in behalf of such corporations, to continue to prosecute suits begun or claims filed previous to such reorganization proceedings and the appointment of a trustee.

The erroneous construction of said statute, if allowed to stand, will have the effect, in the absence of any action by the trustee, of hindering and preventing corporations in reorganization and their stockholders from asserting causes of action under the circumstances above set forth.

The special reason why a reversal of the decision is important to security holders of many railroads now in reorganization arises out of the fact that one of the purposes of the enactment of Section 77 was to do away with the abuses of receivership proceedings by which too often those legally liable for wrecking the railroads escaped all liability. The decision herein tends to continue such evil.

A reversal of the decision is important to St. Louis Southwestern because the claim constitutes a valuable asset of that company. This appears from the record in the case. Additional proof as to this is shown by the action of the United States in the appeal by petitioner and others to the Circuit Court of Appeals for the Eighth Circuit from the decision of the District Court approving

the plan of reorganization of St. Louis Southwestern, *In re St. Louis Southwestern Ry. Co.*, 53 F. Supp. 914.

In March 1945 the Government, through its Attorney General, filed a brief as *amicus curiae* in the said appeal, in which it asked that the claim of Southern Pacific as a creditor in the principal amount of $17,882,250, and as a stockholder owning 87% of the stock of St. Louis Southwestern, be subordinated to the interest of the minority stockholders on the ground that the control exercised by Kansas City Southern over St. Louis Southwestern was unlawful, and "that the debtor had a valuable cause of action for triple damages under the antitrust laws which it was prevented from bringing during its subsequent control by Southern Pacific." Rock Island was a co-conspirator with Kansas City Southern and others in the illegal control exercised over St. Louis Southwestern by Kansas City Southern referred to in the Government's brief, and petitioner so alleged in the claim filed herein.

In view of the meritorious and substantial nature of the claim, if the decision of the Circuit Court of Appeals herein is allowed to stand it will work a grave injustice to St. Louis Southwestern and to the many thousands of its security holders.

WHEREFORE, your petitioner prays that a writ of certiorari be issued out of and under the seal of this Honorable Court, directed to the United States Circuit Court of Appeals for the Seventh Circuit, commanding said Court to certify and send to this Court on a day certain to be therein named, a full and complete transcript of the record and all proceedings in the case numbered and entitled on its docket, No. 8585, In the Matter of: The Chicago, Rock Island and Pacific Railway Company, Debtor; Walter E. Meyer, Appellant, vs. Joseph B. Fleming and Aaron Colnon, as Trustees of The Chicago, Rock Island and Pacific Railway Company, Appellees, to the

end that this cause may be reviewed and determined by this Honorable Court, and that the judgment of the said Circuit Court of Appeals be reversed; and that your petitioner have such other and further relief as may seem proper.

Dated, New York, August 30, 1945.

WALTER E. MEYER,
Petitioner, *Pro Se.*

SONNENSCHEIN, BERKSON, LAUTMANN,
LEVINSON & MORSE,
Attorneys for Petitioner.

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Respondents.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

The Opinions of the Courts Below

The opinion of the Circuit Court of Appeals (R. 61-65) is reported in 149 F. (2d) 529.

The opinion of the District Court (R. 49-52) is not reported.

Statement

The statement of the case set forth in the petition under the heading "Statement of Matter Involved" is hereby adopted and made part of this brief.

Specification of Errors

The Circuit Court of Appeals erred:

1. In affirming the order of the District Court holding that petitioner had no right to continue to prosecute the claim herein and disallowing the claim.

2. In holding, upon the objections of the respondents that all causes of action belonging to St. Louis Southwestern vested in the trustee of that company, that petitioner, a stockholder of St. Louis Southwestern, without any action on the part of said trustee to take over or restrain the prosecution of the claim, was precluded from continuing to prosecute the claim which was filed by him for the benefit of that company in the Rock Island reorganization proceedings previous to the institution of reorganization proceedings of St. Louis Southwestern.

3. In holding that, because under subsection (a) of Section 77 of the Bankruptcy Act the reorganization court is given "exclusive jurisdiction of the debtor and its property wherever located" and "in addition to the powers conferred by this section all the powers, not inconsistent with this section, which a Federal court would have had if it had appointed a receiver in equity of the property of the debtor for any purpose," on that account petitioner, after the institution of reorganization proceedings and the appointment of a trustee for St. Louis Southwestern, was precluded from continuing to prosecute the claim.

4. In holding that because under subsection (c)(2) of Section 77 the trustee of St. Louis Southwestern was given "all the title" and "all of the powers of a trustee appointed pursuant to Section 72 or any other section of this title [11 U. S. C. A.], and, to the extent not inconsistent with this section, if authorized by the judge, the powers of a receiver in an equity proceeding," on that account petitioner was precluded from prosecuting the claim.

5. In failing to take into consideration subsection (*l*) of Section 77, which sets forth that in railroad reorganization proceedings "the jurisdiction and powers of the court, the duties of the debtor and the rights and liabilities of creditors, and all persons with respect to the debtor and its property, shall be the same as if a voluntary petition for adjudication had been filed," and by reason of the failure to do so, holding that petitioner was precluded from prosecuting the claim.

ARGUMENT

A stockholder who filed a claim for the benefit of his railroad in the reorganization proceedings of another railroad is not precluded from continuing to prosecute the claim by reason of the subsequent reorganization proceedings of his railroad and the appointment of a trustee therein, there being no action on the part of that trustee to take over or restrain the prosecution of the claim.

The Circuit Court of Appeals held, upon the objections of the respondents, that by virtue of subsections (a) and (c)(2) of Section 77 of the Bankruptcy Act, petitioner had no right to continue to prosecute a claim filed by him as a stockholder of St. Louis Southwestern for the benefit of said company in the Rock Island reorganization proceedings (R. 66).

The claim had been filed previous to the initiation of the proceedings for reorganization and the appointment of a trustee for St. Louis Southwestern, and said trustee had made no step whatsoever to take over the claim or to enjoin its prosecution by petitioner.

Petitioner submits that under these circumstances the appointment of a trustee for St. Louis Southwestern could not be pleaded by the respondents as a defense to the claim.

It is settled law that if the trustee has not taken over or endeavored to enjoin the prosecution of a suit brought by a bankrupt, and pending at the time of the bankruptcy, it may not be pleaded as a defense that the appointment of the trustee vested such title in him as to abate the suit:

Johnson v. *Collier*, 222 U. S. 538, 540;
Paradise v. *Vogtlandische Maschinen-Fabrik*, (C. C. A. 3), 99 F. (2d) 53, 55;
Bluegrass Canning Co. v. *Steward* (C. C. A. 6), 175 Fed. 537, 543-544;
Thatcher v. *Rockwell*, 105 U. S. 467, 470;
Van der Stegen v. *Neuss, Hesslein & Co.*, 270 N. Y. 55, 59-60;
Bennett v. *Associated Theaters*, 247 Mich. 493, 496;
Griffin v. *Mutual Life Ins. Co.*, 119 Ga. 664, 665;
Collier on Bankruptcy, 14th ed., vol. 1, pp. 1173, *et seq.*

It is also the law that if a receiver in equity under similar circumstances does not act, it may not be pleaded by way of defense that the appointment of the receiver abates the suit:

Boston Elevated Ry. Co. v. *Paul Boyton Co.*, (C. C. A. 1), 211 Fed. 812, 822-823;

Missouri, K. & T. Trust Co. v. *German Nat. Bank* (C. C. A. 8), 77 Fed. 117, 122-123;
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Grimes Savings Bank v. *McHarg*, 217 Iowa 636, 640.

There is no valid reason for any distinction in the application of this rule between a suit brought by a corporation and a suit brought by a stockholder for the benefit of his corporation, and the rule has been applied accordingly in stockholder's suits. *Friederich W. Meyer* v. *Page*, 112 App. Div. (N. Y.) 625; *McAnarney* v. *Lembeck*, 97 N. J. Eq. 361.

The Circuit Court of Appeals herein held that the jurisdiction and power conferred upon the reorganization court under Section 77 of the Bankruptcy Act, including subsection (a) which confers upon the court "exclusive jurisdiction of the debtor and its property wherever located", served to differentiate the law in reorganization proceedings from the law in the ordinary bankruptcy or equity receivership in such a way as to preclude the continued prosecution of the claim herein.

In this the Circuit Court of Appeals erred.

The bankruptcy court has always had exclusive jurisdiction of the bankrupt estate, and upon adjudication title to the property of the bankrupt has vested in the trustee, whether such property was situated within or without the district in which the bankruptcy court sat. *Isaacs* v. *Hobbs Tie & Timber Co.*, 282 U. S. 734, 737. See also *Ex Parte Baldwin*, 291 U. S. 610, 615.

Section 77 relating to the reorganization of railroad corporations was enacted in 1933. Section 77B relating to the reorganization of non-railroad corporations was en-

acted in 1934. The provision giving the court the powers of a Federal court which had appointed a receiver first appeared in subsection (a) of Section 77B.

In 1935 Section 77 was amended, Congress adopting recommendations contained in a report made in 1934 by the late Joseph B. Eastman, Federal Coordinator of Transportation (House Doc. 89, 74th Cong., 1st. Sess.). Mr. Eastman referred to the enactment of Section 77B in 1934, stating that it was based "upon Section 77, but incorporated many minor changes" which "where appropriate, should be adopted" (pp. 102-103). Included in the amendments to Section 77 was the provision of subsection (a) conferring upon the court the powers of a Federal court which had appointed a receiver. The provision, "Process of the court shall extend to and be valid when served in any judicial district," and the provision for the promulgation by the Supreme Court of rules relating to the service of process outside the judicial district, were also added at this time.

Subsection (a) should be read together with subsection (*l*) of Section 77 which provides:

> "In proceedings under this section and consistent with the provisions thereof, the jurisdiction and powers of the court, the duties of the debtor and the rights and liabilities of creditors, and of all persons with respect to the debtor and its property, shall be the same as if a voluntary petition for adjudication had been filed and a decree of adjudication had been entered on the day when the debtor's petition was filed."

The statement that the rights "of all persons with respect to the debtor and its property, shall be the same as if a voluntary petition for adjudication had been filed" would indicate that it was the intention of Congress to guard against the kind of misconstruction of the statute of which the decision of the Circuit Court of Appeals herein is an example.

After the enactment of subsection (a) of Section 77 in its original form, declaring that the reorganization court shall "have exclusive jurisdiction of the debtor and its property wherever located," without, however, the additions thereto subsequently enacted, the Supreme Court in *Ex Parte Baldwin,* 291 U. S. 610, discussed at length (pp. 615 *et seq.*) the jurisdiction of the court.

In that case the trustees of the Missouri Pacific Railroad System, in reorganization in Missouri under Section 77, petitioned the Supreme Court for a writ of mandamus to compel the Federal court for Southern Texas, upon their petition for removal, to take jurisdiction of a suit brought against them in a Texas state court. In holding that the existence of a remedy by injunction of the court in which proceedings for reorganization were pending against the prosecution of the suit in the state court required the denial of the petition for mandamus, the Supreme Court stated that a bankruptcy court had exclusive jurisdiction, and that it could not only issue all writs necessary to protect its possession from physical interference, but was entitled to determine all questions respecting the same; that the jurisdiction was exclusive of the jurisdiction of other courts, and this "regardless of whether the property was located in the district in which the bankruptcy proceeding originated."

The Court in its opinion did not specifically refer to the language in subsection (a) as to the exclusive jurisdiction of the reorganization court. It rested its argument upon the general principle that where a court of competent jurisdiction takes property into its possession, the property is thereby withdrawn from the jurisdiction of other courts (p. 615).

In *Continental Illinois National Bank & Trust Co.* v. *Chicago, R. I. & P. Ry. Co.*, 294 U. S. 648, the Supreme Court construed subsection (a) without the amendments, holding that the bankruptcy court in granting an injunc-

tion to safeguard conceded assets of the trust estate outside its district "was well within its power, either as a virtual court of equity, or under the broad provisions of § 2 (15) of the Bankruptcy Act or of § 262 of the Judicial Code, U. S. C. title 28, § 377" (p. 676). The Court discussed the propriety as distinct from the power of the bankruptcy court to take such action, and held that the injunction was "within the contemplation of § 77, and we need not inquire whether it would be admissible under the act in force prior to the adoption of that section" (p. 677).

In *Thompson* v. *Magnolia Petroleum Co.*, 309 U. S. 478, the Supreme Court again discussed the meaning of exclusive jurisdiction in a railroad reorganization case (p. 483), citing *Isaacs* v. *Hobbs Tie & Timber Co.*, 282 U. S. 734, *supra*, and made no reference to the language in subsection (a) of Section 77.

See also *Warren* v. *Palmer*, 310 U. S. 132.

It is apparent from these decisions that in the opinion of the Supreme Court the language of subsection (a) worked no such radical modification in the jurisdiction hitherto exercised by the bankruptcy court as would appear from the opinion of the Circuit Court of Appeals herein.

Subsection (a) in its amended form was construed in *Thompson* v. *Terminal Shares* (C. C. A. 8), 104 F. (2d) 1, cert. denied 308 U. S. 559.

The question there involved was whether the railroad reorganization court had jurisdiction to entertain a suit against non-resident defendants, involving property outside the district held adversely to the bankrupt estate. It was held that the court was without power to entertain such a suit.

The Court held, Judge Sanborn writing, that the jurisdiction conferred by Section 77 was to be considered

"the traditional jurisdiction" of the bankruptcy court "over the property of a bankrupt, wherever located, freed, however, from those limitations which made ancillary proceedings in other districts necessary, and with the powers which Federal equity courts exercise in receivership proceedings, so far as those powers may be necessary or appropriate in order to preserve and safeguard the property in the actual or constructive possession of debtors and in order to carry on their business pending reorganization" (p. 9).

The language of subsection (a), Judge Sanborn stated, should be considered in connection with subsection (*l*) of Section 77, and must be "read in the light of the legislative history of Section 77 and of long established Congressional policy" (pp. 4-5).

He pointed out that while the *Continental Illinois National Bank & Trust Co.* case (*supra*) was pending in the Supreme Court, there being doubt as to its decision, the provision was added which gave the court the powers "not inconsistent with this section, which a Federal court would have had if it had appointed a receiver in equity," and also the provisions rendering the process of the court valid in jurisdictions other than in the reorganization court district.

Referring to the report of Mr. Eastman on which the amendments to Section 77 were based, Judge Sanborn stated that that report nowhere contained any suggestion that "the proposed amendments relating to jurisdiction were intended to confer any additional powers upon the courts of bankruptcy with respect to the reorganization of railroads" (p. 7).

In addition to subsection (a), the Circuit Court of Appeals herein also relied on subsection (c)(2) of Section 77, to the effect that the trustee "shall have all the title and shall exercise • • • all of the powers of a trustee

appointed pursuant to section 72* or any other section of this title [11 U. S. C. A.], and, to the extent not inconsistent with this section, *if authorized by the judge*, the powers of a receiver in an equity proceeding."

The trustee in his title to the debtor's property and in his powers is necessarily limited by the jurisdiction and powers of the court of which he is an officer.

Moreover, Section 72 (of 11 U. S. C. A.) has to do with the appointment of trustees in ordinary bankruptcy proceedings. The trustee under Section 77 by these words is thus given no more power than is given to a trustee in the ordinary bankruptcy proceeding.

As to "the powers of a receiver in an equity proceeding" "to the extent not inconsistent with this section", which, as appears from the above language of the statute, it is left entirely to the discretion of the judge to withhold from or to confer upon the trustee, there is nothing in the record to show that the reorganization court gave such powers to the St. Louis Southwestern trustee. But assuming that the trustee had been given the powers of a receiver, inasmuch as the appointment of a receiver does not preclude the continued prosecution of a suit under the circumstances of this case (see p. 12, *supra*), it follows that conferring upon the trustee the powers of a receiver could not do so.

It is expressly stated in subsection (c) (2), that the title and powers given the trustee shall be given to the extent *not inconsistent with Section 77*. In view of the fact that subsection (*l*) of Section 77 provides that the rights "of all persons with respect to the debtor and its property, shall be the same as if a voluntary petition for adjudication had been filed", it is plain that any title

* Section 72 of 11 U. S. C. A. is reproduced in full in the Appendix, pages 29-30.

or any powers conferred upon the trustee could in no way affect the right of the petitioner to continue to prosecute the claim.

Section 77B contained language similar to that in Section 77 (a), (c)(2) and (*l*) herein discussed, the corresponding subsections of Section 77B being (a), (c)(2) and (o).* The substance of these provisions of former Section 77B was retained in Chapter X of the Bankruptcy Act (See Sections 111, 115, 186, 187, 112, 114 and 200.)*

The language in Section 77B as to the jurisdiction of the court was construed in *In re Prudence Bonds Corp.* (C. C. A. 2), 75 F. (2d) 262, 263; *In re Prudence Co.* (C. C. A. 2), 96 F. (2d) 157, 159, cert. denied 305 U. S. 616; *United States* v. *Tacoma Oriental S. S. Co.* (C. C. A. 9), 86 F. (2d) 363, 368; and *In re Standard Gas & Electric Co.* (C. C. A. 3), 119 F. (2d) 658, 661.

In *In re Prudence Bonds Corp.*, 75 F. (2d) 262, which is referred to by the Circuit Court of Appeals herein (R. 64), after the appointment of trustees of the Prudence Corporation under Section 77B, a holder of a Prudence note filed a suit in a state court against the indenture trustee for an accounting of income from the pledged mortgages. The reorganization court stayed the prosecution of the suit on the petition of the indenture trustee. The Circuit Court of Appeals for the Second Circuit, consisting of Judges Learned Hand, Swan and Chase, Judge Hand writing, construed the language in Section 77B (a) as to exclusive jurisdiction and also Section 77B (o) (corresponding to subsection (*l*) of Section 77), stating (p. 263):

> "It is clear both from the language used in these subdivisions, and from the consequences of a contrary ruling, that Congress did not intend the bankruptcy court in proceedings under Section 77B to

*Reprinted in the Appendix, pages 27-29.

take over all litigation between the debtor and third persons."

The opinion of the Circuit Court herein (R. 64) fails to bring out that the stay in the said *Prudence* case was granted by the *reorganization court* on the ground that the suit would interfere with its disposition of the estate. The assertion of the claim herein in no wise interferes with the St. Louis Southwestern reorganization proceedings, nor has the St. Louis Southwestern reorganization court enjoined the continued prosecution of the claim.

Later, in *In re Prudence Co.*, 96 F. (2d) 157, the Circuit Court of Appeals for the Second Circuit allowed a pending suit to be continued after the appointment of the trustees. The matter came up before Judges Manton, Swan and Chase, two of whom, as has been indicated, participated in the decision in *In re Prudence Bonds Corp., supra.* The trustees had proposed that the attorney who acted for the bankrupt become their attorney and continue the litigation, his compensation to be determined by the bankruptcy court. This proposal the attorney declined to accept, continuing the litigation in the name of the corporation on the basis of his original retainer. The Circuit Court (p. 159) held that the filing of the petition did not terminate his employment nor stay the pending suit; that while under 11 U. S. C. A., Section 29 (c), the trustees had the right to take over the prosecution of the suit, they also had the right to allow the suit to be continued by the bankrupt and later claim the fruits of any recovery. The Court continued:

> "In the case at bar the debtor's trustees chose the latter course. They did not intervene in the pending suit, nor employ Mr. Davison as their attorney; they merely allowed him to perform his contract of retainer with the debtor."

The decision of the Circuit Court of Appeals for the Second Circuit in *Meyer* v. *Kansas City Southern*, a suit

brought by this petitioner as a stockholder of St. Louis Southwestern for the benefit of that company, supports the position taken by him herein. In that case the District Court for the Southern District of New York on September 6, 1935, dismissed the complaint, not on the merits but on the ground that the court did not have subject matter jurisdiction. St. Louis Southwestern filed its petition for reorganization on December 12, 1935, and a trustee was appointed on January 3, 1936 (R. 50). The Circuit Court of Appeals in its decision, rendered on June 22, 1936, refers to the appointment of a trustee of St. Louis Southwestern (p. 414), but does not suggest that such appointment abated the representative action brought by petitioner and thus prevented the prosecution of the appeal. *Meyer* v. *Kansas City Southern*, 84 F. (2d) 411, aff'g 11 F. Supp. 937, cert. denied 299 U. S. 607.*

The decision of the Circuit Court of Appeals herein is clearly in conflict with the decision of the Circuit Court of Appeals for the Second Circuit in *In re Prudence Co.*, 96 F. (2d) 157, the dictum of that court in *In re Prudence Bonds Corporation*, 75 F. (2d) 262, and its decision in *Meyer* v. *Kansas City Southern*, 84 F. (2d) 411; and is probably in conflict with the decision of the Circuit Court of Appeals for the Eighth Circuit in *Thompson* v. *Terminal Shares*, 104 F. (2d) 1, for the Ninth Circuit in *United States* v. *Tacoma Oriental S. S. Co.*, 86 F. (2d) 363, and for the Third Circuit in *In re Standard Gas & Electric Co.*, 119 F. (2d) 658.

The Circuit Court of Appeals was under a misapprehension in stating that petitioner contended that, because "the procedure in interstate railroad reorganization under § 77 is substantially that of an equity receivership the

* Though it does not appear in the record herein, the fact is that after the appointment of the trustee the St. Louis Southwestern moved to stay the appeal. The Circuit Court of Appeals refused to grant the stay. The appeal was argued May 20, 1936.

appointment of the trustee did not prevent the continued prosecution" of the claim herein (R. 63). Nor did petitioner cite the cases there listed in the margin in support of such contention. Petitioner's contentions before the Circuit Court and the cases cited by him in support thereof do not differ from those set forth in this brief, save that in this brief, he has cited some additional cases.

As has been shown, where suits have been begun before the appointment of a trustee or receiver the courts have not allowed a defendant to plead the appointment of the trustee or receiver as a defense.

Porter v. *Sabin*, 149 U. S. 473; *Klein* v. *Peter*, 284 Fed. 797; and *Kelly* v. *Dolan*, 233 Fed. 635, cited by the Circuit Court of Appeals herein (R. 65), were all cases where a stockholder brought suit *after* the appointment of a receiver for the corporation. *Reagan* v. *Midland Packing Co.*, 8 F. (2d) 954, also cited by the Court (R. 65), was a case where a judgment-creditor of a corporation brought suit *after* a receiver had been appointed.

The Circuit Court cites *Adler* v. *Seaman*, 266 Fed. 828, and *Seaman* v. *McCulloch*, 8 F. (2d) 820, as indicating the necessity of the court's passing upon the desirability of proceeding with a suit (R. 65).

The facts in these cases were that while a stockholder's suit was pending in the District Court, seeking the appointment of a receiver of the corporation and injunctive relief against the directors, a bondholder brought suit in the same court also asking for the appointment of a receiver. The company contested the stockholder's suit, but consented to the appointment of a receiver in the bondholder's suit. The Court allowed the two suits to be consolidated. The Circuit Court of Appeals reversed on the ground that the consolidation was improper. Thereafter the representative action brought by the stockholder was dismissed.

In the *Seaman* cases the facts were wholly different from the facts in this case. In *Seaman* v. *McCulloch*, the Circuit Court stated (p. 826) that the recovery sought in the stockholder's action was involved with certain power contracts and that the receiver's "functioning might be vitally affected by the disposition of these contracts." Moreover, the Court stated that the appointment of the receiver "did not *ipso facto, et eo instanti*, abate" the stockholder's action. The instant claim is not against St. Louis Southwestern and its directors. It was filed by petitioner in the Rock Island reorganization court and is for the benefit of St. Louis Southwestern. It can in no way be said to be interfering with the functioning of the trustee of St. Louis Southwestern.

It is a matter of importance to all corporations in reorganization and their security holders that the decision herein be reversed, and that the rule which permits the continued prosecution of a suit or claim under the circumstances previously outlined should continue in effect.

That rule is supported by practical considerations. The trustee or receiver in equity has the power to take over the prosecution of the suit or claim, but he may choose not to do so. This may be because he believes that the chances of success are not good and he does not desire to incur the expense of what he considers will be fruitless litigation (*Johnson* v. *Collier*, 222 U. S. 538, at p. 540; *Paradise* v. *Vogtlandische Maschinen-Fabrik* (C. C. A. 3), 99 F. (2d) 53, at p. 55), or for other reasons; *In re Prudence Co.* (C. C. A. 2), 96 F. (2d) 157; *Bluegrass Canning Co.* v. *Steward* (C. C. A. 6), 175 Fed. 537).

Often the trustee may not have the intimate knowledge of the facts or the zeal and persistence necessary for the successful prosecution of arduous litigation, or he may be reluctant to undertake litigation against those connected with the management of the corporation or against others. Such a trustee may not be willing ex-

pressly to authorize the continued prosecution of a suit by the corporation or a stockholder; yet he may also be unwilling to take the responsibility of restraining its prosecution.

Under the rule that has hitherto prevailed, as has been brought out, causes of action constituting valuable assets, which would otherwise be lost, are thus preserved. In the event of a recovery, all the benefits accrue to the bankrupt estate or corporation in receivership and this without the trustee or receiver incurring the often heavy burden and expense involved in the conduct of the litigation.

There are special reasons why a reversal of the decision is important to the many railroads now in reorganization and to their security holders.

Among the purposes of the enactment of Section 77 was the elimination of the abuses of equity receivership proceedings by which those legally liable for the wrecking of railroads too often escaped all liability (72nd Cong., 2d Sess., Cong. Rec., Vol. 76, pp. 2916, 4887, 5358). The decision herein is contrary to this purpose of the statute, and will be a source of encouragement to powerful financial interests in continuing to flout the law.

The claim filed by your petitioner constitutes a valuable asset to St. Louis Southwestern which will be lost if the decision is allowed to stand. Its meritorious and substantial nature is apparent from the allegations of petitioner in his proof of claim (R. 2-7); his Reply to the "New Matter in Support of Objections" filed by the Rock Island trustees (R. 10-15); and the dissenting opinion of Chairman Eastman in *St. Louis S. W. Ry. Co. Reorganization*, 249 I. C. C. 5, at page 177 *et seq.* (R. 15-33).

In his dissent Chairman Eastman showed that he was of the opinion that petitioner in the hearings before the Interstate Commerce Commission in the St. Louis Southwestern reorganization proceedings to a very large extent

had sustained the charges in his petition for investigation as to the illegal and wrongful control exercised over St. Louis Southwestern, and that the Commission should have granted the said petition. Referring to the part played by Rock Island in the undoing of St. Louis Southwestern, the Chairman stated that the downfall of St. Louis Southwestern began when Rock Island first acquired a dominant stock interest in the property in March 1925 (R. 17).

The United States, through the Attorney General, has recorded its belief in petitioner's charges in respect to the illegal control exercised over St. Louis Southwestern in filing a brief as *amicus curiae* in the appeal now pending in the Circuit Court of Appeals for the Eighth Circuit from the decision of the District Court approving the Commission's plan of reorganization of St. Louis Southwestern. The Government asks that because Southern Pacific, a large creditor and controlling stockholder of St. Louis Southwestern, did not permit that company to assert the cause of action which it had against Kansas City Southern, Southern Pacific should be subordinated to the interest of the minority stockholders in the plan of reorganization of St. Louis Southwestern (Petition, pp. 6-7). As appears from the claim herein, petitioner charged that Southern Pacific and Rock Island were co-conspirators with Kansas City Southern in the illegal control exercised by Kansas City Southern over St. Louis Southwestern by which St. Louis Southwestern was damaged (R. 4).

For all of the foregoing reasons, the petition for a writ of certiorari should be granted.

Dated: New York, August 30, 1945.

Respectfully submitted,

WALTER E. MEYER,
Petitioner *Pro Se.*

SONNENSCHEIN, BERKSON, LAUTMANN,
LEVINSON & MORSE,
Attorneys for Petitioner.

Appendix.

The pertinent provisions of Section 77 of the Bankruptcy Act (11 U. S. C. A. 205) are as follows:

"(a) * * * If the petition is so approved, the court in which such order is entered shall, during the pendency of the proceedings under this section and for the purposes thereof, have exclusive jurisdiction of the debtor and its property wherever located, and shall have and may exercise in addition to the powers conferred by this section all the powers, not inconsistent with this section, which a Federal court would have had if it had appointed a receiver in equity of the property of the debtor for any purpose. Process of the court shall extend to and be valid when served in any judicial district. The Supreme Court of the United States shall promulgate rules relating to the service of process outside of the district in which the proceeding is pending; and any other rules which it may deem advisable in order to aid district courts and circuit courts of appeal in exercising the jurisdiction herein conferred upon them. * * *"

"(c)(2) * * * The trustee or trustees so appointed, upon filing such bond, shall have all the title and shall exercise, subject to the control of the judge and consistently with the provisions of this section, all of the powers of a trustee appointed pursuant to section 72 or any other section of this title, and, to the extent not inconsistent with this section, if authorized by the judge, the powers of a receiver in an equity proceeding, and, subject to the control of the judge and the jurisdiction of the Commission as provided by chapter 1 of Title 49 as on August 27, 1935, or thereafter amended, the power to operate the business of the debtor. * * *"

"(*l*) In proceedings under this section and consistent with the provisions thereof, the jurisdiction and powers of the court, the duties of the debtor and the rights and li-

abilities of creditors, and of all persons with respect to the debtor and its property, shall be the same as if a voluntary petition for adjudication had been filed and a decree of adjudication had been entered on the day when the debtor's petition was filed."

The corresponding provisions of Section 77B of the Bankruptcy Act (11 U. S. C. A. 207) were as follows:

"(a) * * * If the petition or answer is so approved, an order of adjudication in bankruptcy shall not be entered and the court in which such order approving the petition or answer is entered shall, during the pendency of the proceedings under this section, have exclusive jurisdiction of the debtor and its property wherever located for the purposes of this section, and shall have and may exercise all the powers, not inconsistent with this section, which a Federal court would have had it appointed a receiver in equity of the property of the debtor by reason of its inability to pay its debts as they mature. * * *"

"(c)(2) * * * every such trustee, upon filing such bond, shall have all the title and shall exercise, subject to the control of the judge and consistently with the provisions of this section, all the powers of a trustee appointed pursuant to section 72 of this Act, and if authorized by the judge, the same powers as those exercised by a receiver in equity to the extent consistent with this section, and, subject to the authorization and control of the judge, the power to operate the business of the debtor during such period, fixed or indefinite, as the judge may from time to time prescribe;"

"(o) In proceedings under this section and consistent with the provisions thereof, the jurisdiction and powers of the court, the duties of the debtor and the rights and liabilities of creditors, and of all persons with respect

to the debtor and its property, shall be the same as if a voluntary petition for adjudication had been filed and a decree of adjudication had been entered on the day when the debtor's petition or answer was approved."

The corresponding provisions of Chapter X of the Bankruptcy Act (Sections 111, 113, 186, 187, 112, 114, 200) (11 U. S. C. A. 511, 513, 586, 587, 512, 514, 600) are as follows:

§ 511. ***Exclusive jurisdiction over debtor and property.*** Where not inconsistent with the provisions of this chapter, the court in which a petition is filed shall, for the purposes of this chapter, have exclusive jurisdiction of the debtor and its property, wherever located.

§ 513. ***Jurisdiction as in insolvency.*** Upon the approval of a petition, the court shall have and may, in addition to the jurisdiction, powers, and duties hereinabove and elsewhere in this chapter conferred and imposed upon it, exercise all the powers, not inconsistent with the provisions of this chapter, which a court of the United States would have if it had appointed a receiver in equity of the property of the debtor on the ground of insolvency or inability to meet its debts as they mature.

§ 586. ***Trustee; title.*** A trustee, upon his appointment and qualification, shall be vested with such title as a trustee appointed under section 72 of this title would have.

§ 587. ***Same; rights, powers, and duties.*** Where not inconsistent with the provisions of this chapter, a trustee, upon his appointment and qualification, shall be vested with the same rights, be subject to the same duties, and exercise the same powers as a trustee appointed under section 72 of this title, and, if authorized by the judge, shall have and may exercise such additional rights and powers as a receiver in equity would have if appointed

by a court of the United States for the property of the debtor.

§ 512. *Matters prior to approval of petition; jurisdiction, powers and duties.* Prior to the approval of a petition, the jurisdiction, powers, and duties of the court and of its officers, where not inconsistent with the provisions of this chapter, shall be the same as in a bankruptcy proceeding before adjudication.

§ 514. *Matters upon approval of petition; jurisdiction, powers, and duties.* Upon the approval of a petition, the jurisdiction, powers, and duties of the court and of its officers, where not inconsistent with the provisions of this chapter, shall be the same as in a bankruptcy proceeding upon adjudication.

§ 600. *Rights, duties, and liabilities of creditors, etc.* Where not inconsistent with the provisions of this chapter, the rights, duties, and liabilities of creditors and of all other persons with respect to the property of the debtor shall be the same, before the approval of the petition, as in a bankruptcy proceeding before adjudication and, upon the approval of the petition, as in a bankruptcy proceeding upon adjudication.

Section 44 of the Bankruptcy Act (11 U. S. C. A. 72) reads as follows:

"(a) The creditors of a bankrupt, exclusive of the bankrupt's relatives or, where the bankrupt is a corporation, exclusive of its stockholders or members, its officers, and the members of its board of directors or trustees or of other similar controlling bodies, shall, at the first meeting of creditors after the adjudication, or after a vacancy has occurred in the office of trustee, or after an estate has been reopened, appoint a trustee or three trustees of such estate. If the creditors do not appoint

a trustee or if the trustee so appointed fails to qualify as herein provided, the court shall make the appointment. If the bankrupt is a face-amount certificate company, as defined in section 80a—4 of Title 15, the court alone shall make the appointment; but the court shall not make such appointment without first notifying the Securities and Exchange Commission and giving it an opportunity to be heard.

"(b) Such creditors may, at their first meeting, also appoint a committee of not less than three creditors, which committee may consult and advise with the trustee in connection with the administration of the estate, make recommendations to the trustee in the performance of his duties and submit to the court any question affecting the administration of the estate.

"(c) An attorney shall not be disqualified to act as attorney for a receiver or trustee merely by reason of his representation of a general creditor."